

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

HAMILTON SECURITIES ADVISORY
SERVICES, INC.

Plaintiff,

v.

UNITED STATES OF AMERICA,

Defendant.

CASE NO. 98-169C
(Judge Horn)

**PLAINTIFF'S RESPONSE TO
DEFENDANT'S MOTION TO DISMISS
FOR LACK OF SUBJECT MATTER JURISDICTION**

June 25, 1998

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COMES NOW, Plaintiff, Hamilton Securities Advisory Services, Inc. ("Hamilton"), and responds to Defendant's Motion to Dismiss for Lack of Subject Matter Jurisdiction. As shown below, the Court plainly has jurisdiction in this case. Accordingly, the Defendant's motion must be denied.

INTRODUCTION

In this suit, Hamilton appeals two decisions of the contracting officer: (1) the contracting officer's constructive denial of Hamilton's December 10, 1997, claim for payment of outstanding invoices; and (2) the contracting officer's final decision asserting a government claim for "at least \$3.8 million" against Hamilton. The government has moved to dismiss for lack of jurisdiction, contending that no predicate final decision on Hamilton's claims was, or could have been, issued

because the claims were in litigation in another court.¹ As demonstrated below, however, this Court has jurisdiction over both claims.

It has jurisdiction over HUD's claim against Hamilton pursuant to Placeway Construction Corp. v. United States, 920 F.2d 903 (Fed.Cir. 1990), because the contracting officer's October 17, 1997, demand for payment of \$3.8 million constituted a final decision on a government claim. The Court separately has jurisdiction over Hamilton's December 10, 1997 claim for \$1.5 million, because the contracting officer constructively denied it before the district court litigation was filed by refusing Hamilton's October 22 and November 13, 1997 claims for release of the funds. Kit-San-Azusa, J.V. v. United States, 32 Fed.Cl. 647, 664 (1995). None of those claims was pending before the district court when this suit was filed. Finally, the district court did not bar the contracting officer's constructive denial of Hamilton's December 10, 1997 claim because the district court action involved conceptually different claims based on statutory and constitutional grounds -- and not founded on contract. Accordingly, the Court properly has jurisdiction, and it should deny the government's motion.

STATEMENT OF FACTS

Hamilton performed work in September and October 1997 under a contract with the U.S. Department of Housing and Urban Development ("HUD"), for which it

¹ Since the government contests jurisdiction here, it obviously does not allege any fraud. Government counterclaims based on fraud are "excluded from the specific jurisdictional prerequisite of a contracting officer's final decision established by section 605(a) of the CDA." Sharman Co., Inc. v. United States, 2 F.3d 1564, 1568 n. 5 (Fed.Cir. 1993); Simko Construction, Inc. v. United States, 852 F.2d 540, 546 (Fed.Cir. 1988).

submitted proper invoices totaling \$1,505,265. HUD has acknowledged that it is indebted to Hamilton in the claimed amount. Nevertheless, HUD has wrongfully refused to pay Hamilton's invoices on the basis that it has an alleged offset in the amount of "at least \$3.8 million."

HUD's offset claim is premised on an alleged breach of contract stemming from a discrepancy in the running of a computer model designed to identify the most advantageous set of bids in sales of HUD-held mortgages. HUD received over \$1 Billion in two particular sales – the West of Mississippi and North Central sales – but it claims it might have received \$3.8 million more in those two sales had the computer model discrepancy not existed.

Hamilton disclosed the computer model discrepancy to Nicolas Retsinas (an Assistant Secretary of HUD and the Commissioner of the Federal Housing Administration (the "FHA")) and Kathy Rock (the Comptroller of the FHA and Government Technical Monitor for Hamilton's contract) in December 1996. Although HUD had knowledge of the discrepancy as early as December 1996, it continued to pay Hamilton's invoices until it terminated the contract for convenience ten months later, on October 17, 1997.

On October 17, 1997, the contracting officer also issued a letter demanding that Hamilton make a "voluntary repayment" of \$3,883,551, which the contracting officer stated was the amount of loss HUD suffered as a result of an alleged "performance failure" on Hamilton's part under its contract. (Appendix ("App."), pp.

64-65.)² The letter stated that HUD was "withholding any further payments due and owing Hamilton under the terms and conditions of Contract DU100C000018505 and Task Order 001 until such time as the debt is satisfied." The contracting officer also stated that HUD reserved the right to assert "future claims" for additional losses or damages it might suffer.

On October 22, 1997, Hamilton's attorneys notified the contracting officer that it "vigorously dispute[d]" HUD's claim for set off and demanded resolution of the set off claim and other open issues "once and for all." (App., pp. 66-68.) By letter dated November 13, 1997, Hamilton then requested the contracting officer to defer collection of the \$3.8 million claim and to "cease withholding all payments owed Hamilton under the Contract." (App., pp. 69-71.)

Since HUD took no action, Hamilton submitted a claim in the amount of \$1,505,256 plus interest on December 10, 1997. (App., pp. 72-73.) The amount claimed was the aggregate of the amounts of Hamilton's September and October 1997 invoices (\$868,417 and \$636,839, respectively). HUD later acknowledged that it is indebted to Hamilton in the amount set forth in Hamilton's certified claim. (Exhibit 6 to the Complaint, transcript, pp. 20-21.)

Hamilton continued to press for a reversal of the set off claim in December 1997, since HUD's failure to pay was jeopardizing Hamilton's very existence. Hamilton (and its attorneys) sent urgent letters to the Secretary of HUD (on

² The government's motion had attached to it an Appendix containing 63 pages. For convenience of reference, Hamilton has numbered its Appendix consecutively, beginning with page 64 and running through page 86.

December 22, 1997) and to HUD's Office of General Counsel (on December 22 and 29, 1997) requesting release of the withheld funds. (App., pp. 74-82.) Notwithstanding, HUD's Office of General Counsel advised Hamilton by letter dated December 30, 1997 that HUD was exercising set off rights based on Hamilton's alleged "breach of contract." (App., pp. 83-84.)

Hamilton filed suit on January 8, 1998 in the U.S. District Court for the District of Columbia. In Counts 1 and 2 of its suit, Hamilton sought declaratory and injunctive relief on statutory and constitutional claims relating to HUD's procedural lapses in withholding funds. (App., pp. 45-48.) The substance of the set off claim was not before the district court. Hamilton voluntarily dismissed Counts 1 and 2 on February 17, 1998. (App., pp. 58-59.) The remaining counts against HUD -- including Count 7 (constructive debarment) and Count 8 (due process) -- were voluntarily dismissed on March 4, 1998. (App., pp. 60-62.)

Hamilton filed suit in this Court on March 9, 1998, alleging two breaches by HUD. First, it alleged that "HUD's failure to pay Hamilton's September and October invoices was wrongful and in breach of contract." (Complaint ¶ 24.) It then separately alleged that HUD had no contractual or legal basis for asserting its claim for \$3.8 million and that "HUD's withholding of payments on the basis of allegations set forth in its October 17, 1997 letter was wrongful and in breach of contract." (Complaint ¶¶ 21 and 25.)

ARGUMENT

Jurisdiction is not barred by Hamilton's district court litigation. The contracting officer asserted a final claim for \$3.8 million in October 1997, long before the district court action was filed, and this suit was filed after the district court action was dismissed. The contracting officer also constructively denied Hamilton's October 22 and November 13 claims for release of the \$1.5 million the contracting officer was withholding, which had the effect of constructively denying Hamilton's December 10, 1997 claim before the district court action was filed. Finally, since the district court action involved statutory and constitutional claims – and not contract claims – it did not bar the contracting officer from deciding Hamilton's December 10th claim. Accordingly, for all of the above reasons, jurisdiction lies here.

HUD Asserted A Final Claim For \$3.8 Million Against Hamilton

When the contracting officer issued her October 17, 1997 demand letter, she effectively issued a final decision on a government claim against Hamilton. The circumstances here are essentially the same as those presented in Placeway Construction Corp. v. United States, 920 F.2d 903 (Fed.Cir. 1990), where the Federal Circuit found jurisdiction over a set off claim against the contractor. The Federal Circuit found jurisdiction in that case even though the government's demand letter was not labeled "final;" it omitted the boilerplate appeal-rights language, and it indicated the amount claimed "*might*" be reduced later. Since the circumstances here are materially identical, Placeway controls, and jurisdiction exists over HUD's set off claim.

In Placeway, the contractor submitted vouchers for payment of the contract price balance after the work was completed. The government retained the balance, however, because Placeway had not timely completed the work. Placeway then submitted uncertified demands for payment. The contracting officer decided the contract price balance would not be “released” because Placeway’s delays had exposed the government to potential liability on delay claims by other contractors. The decision letter contained neither the label “Final Decision” nor the notice of appeal rights that final decision letters normally contain. Placeway, 920 F.2d at 906. After Placeway filed suit, the Claims Court dismissed, concluding that “because the CO had not yet ascertained the amount of the set off, no final decision was made by the CO, and thus the Claims Court had no jurisdiction to decide the dispute.” Id.

The Federal Circuit reversed, however, reasoning that the contracting officer “effectively made a final decision on the government [set off] claim” when he declined to pay the balance due on the contract. It explained that the finality of the contracting officer’s decision granting the government a sum certain was unaffected by the fact that he “*might*” later decide a different sum was owed. Id. (emphasis in original). The Federal Circuit held as follows:

Accordingly, we conclude that the CO made a final decision on the government claim alleging damages because of Placeway’s delay in contract performance. The decision is no less final because it failed to include boilerplate language usually present for the protection of the contractor. Moreover, the CO’s decision was adverse to Placeway and thus it could properly appeal to the Claims Court.

Id. at 907.

Placeway governs here because the circumstances are precisely the same. Hamilton submitted proper invoices and demands for payment. The contracting officer issued a written decision that neither stated it was a final decision nor included the standard appeal rights. Nevertheless, the contracting officer's written demand determined both liability and damages. It quantified the amount of the set off as a sum certain, and it set forth the purported basis for the withholding – breach of contract. (App., pp. 64-65.)

Moreover, the demand letter properly should be construed as a final decision, since the contracting officer is prohibited from sending a demand letter without first issuing a final decision. "No demand for payment under 32.610 shall be issued prior to a contracting officer's final decision." Federal Acquisition Regulation ("FAR") 32.608(c).³

These circumstances plainly establish that the demand letter was a final decision on a government claim, and they belie any current assertion by the government that the set off decision was not final. Accordingly, the Court has jurisdiction over this appeal from the contracting officer's final decision. Placeway, 920 F.2d at 907.

³ This essentially was the same conclusion that Judge Wiese reached in Sharman Co., Inc. v. United States, 24 Cl.Ct. 763, 768 (1991) (concluding that a separate final decision pursuant to FAR 32.610 is necessary only when the amount is contested and not where underlying liability is disputed). Judge Wiese's decision was overturned in Sharman Co., Inc. v. United States, 2 F.3d 1564 (Fed.Cir. 1993), which was then overruled by Reflectone, Inc. v. United States, 60 F.3d 1572 (Fed.Cir. 1995).

HUD Relies On An Overruled Case

Although the government acknowledges that the October 17th demand letter “potentially could provide a basis for jurisdiction” under Placeway, it suggests that the demand here was non-final, citing Sharman Co. v. United States, 2 F.3d 1564 (Fed.Cir. 1993). (Government Brief, p. 9.) The government’s attempt to distinguish Placeway on the basis of Sharman is unavailing, however, since Sharman has been overruled.

The Court in Sharman concluded that a demand for repayment of progress payments was not final because it invited Sharman to submit a proposal for deferment of collection “if immediate payment is not practicable or if the amount is disputed.” Sharman, 2 F.3d at 1570.⁴ Relying specifically on Dawco Construction, Inc. v. United States, 930 F.2d 872, 878 (Fed.Cir. 1991), the Court concluded that the quoted language prevented the demand for repayment from being final because it invited negotiations on the amount demanded. Dawco held that a claim was not appealable unless both the amount claimed and liability were disputed at the time the claim was submitted.

However, as the government should well know, both Dawco and Sharman were expressly overruled in Reflectone, Inc. v. Dalton, 60 F.3d 1572, 1579 (Fed.Cir. 1995). Indeed, in overruling Sharman the Federal Circuit in Reflectone specifically referred to the part of that case on which the government now relies:

⁴ The same language, which is required by FAR 32.610(b)(3) appeared in the October 17th letter.

Four of our cases followed Dawco by requiring that a CDA "claim" be in dispute when submitted to the CO: Sharman Co., 2 F.3d at 1571 (holding government letter to contractor did not assert a government claim, in part *because amount specified was not yet in dispute*) ..

Reflectone, 60 F.3d at 1579 n. 10 (emphasis added). Consequently, Placeway – and not Sharman – controls here.

Sharman Is Distinguishable Because HUD Conveyed Finality Here

Even if Sharman were good law – which it is not – the facts and circumstances here are distinguishable. In contrast to Sharman and despite the required solicitation of a deferment proposal, the contracting officer's demand letter here was couched in terms reflecting finality. It set forth an unequivocal "demand for payment of the \$3,883,551 loss that the Department suffered as a result of Hamilton's performance failure" and stated that all amounts due would be withheld "until such time as the debt is satisfied." It also stated as follows:

I find this amount [\$3.8 million], at a minimum, represents the monetary loss to HUD as a result of Hamilton's performance failure. However, the Government reserves the right to make future claims against Hamilton to recover any additional losses or damages the Department may suffer or has suffered as a result of Hamilton's failed performance.

(App., pp. 64-65 (emphasis added).) This language simply does not express an interim or tentative decision. Cf. Greenhill Reforestation, Inc. v. United States, 39 Fed.Cl. 683, 687 (1997) (decision was not final because it did not indicate it was invoking claim and it stated amounts were being held only pending investigation).

indeed, the contracting officer could not have had in mind the possibility of "future claims" if she did not consider her letter to be asserting a final "present claim."

The government's actions after October 17th serve to confirm that the contracting officer's decision was final. For example, the contracting officer refused to release the Hamilton funds withheld on the basis of her October 17th letter, despite Hamilton's repeated demands for such action. (App., pp. 66-71.) Hamilton's pleas to other HUD officials similarly fell on deaf ears. (App., pp. 74-82.)

HUD's written communications also confirmed the finality of the October 17th claim. HUD's response to Hamilton's pleas for payment, set forth in a letter from its Office of General, was simply that the set off was proper, "based upon the fact that Hamilton is indebted to HUD due to breach of contract." (App., p. 83.) In fact, as late as March 6, 1997, in a letter signed by Mr. Gottesman, the Department of Justice referred to the October 17, 1997 letter as the "Government's claim." (App., pp. 85-86.) That same letter threatened to hold Hamilton's representatives personally liable if proceeds from a liquidation sale were used for purposes other than "satisfying the Government's claim." (App., p. 86.) This is hardly language indicative of a tentative decision to hold Hamilton liable. These circumstances demonstrate that the government's current pretense -- that the demand was not "final" -- transparently is just a litigation posture taken to delay dealing with the merits of the case.⁵

⁵ This strategy of delay is also apparent in the government's request for extension of time in which to answer or respond. Although counsel represented that additional time was needed to gather relevant information, the motion to dismiss sets forth solely facts and circumstances long known to the government. Since Mr. Gottesman was involved in the district court proceedings, he should have been able to lodge his jurisdictional motion without any time extension.

HUD Constructively Denied Hamilton's Claims For Release Of Its Funds

After receiving the contracting officer's October 17th set off demand letter, Hamilton promptly responded by disputing any liability for the amount claimed by the government and demanding the immediate of funds owed to it. These demands constituted claims for payment, and the contracting officer was required either to issue a final decision on those claims within 60 days or release Hamilton's funds. Since the contracting officer took neither action, she constructively denied those claims. Moreover, even if it were assumed for sake of argument that HUD's October 17th claim were not final – which it was – the contracting officer's failure to release the funds in the face of Hamilton's claims effectively rendered it final.

By letter dated October 22, 1997, Hamilton, by its attorneys, demanded immediate resolution of open issues "once and for all," and stated as follows:

Hamilton vigorously disputes the Government claim. It is apparent from the face of your [October 17th] letter that HUD did not discharge its duty to determine the contractual validity of the "debt" before asserting it. HUD's withholding contract payments otherwise due Hamilton, therefore, is improper.

(App., p. 66.) By definition, this letter constituted a claim, since it (i) certainly was not a routine submission, (ii) was addressed to the contracting officer, (iii) requested the adjustment of contract terms or other relief under the contract, and (iv) clearly communicated a desire for a final decision. James M. Ellett Construction Co., Inc. v. United States, 93 F.3d 1537, 1543 (Fed.Cir. 1996).

Since the October 22nd letter was a claim, the contracting officer was obligated to issue a decision on it within 60 days. 41 U.S.C. § 605(c)(5). The contracting officer, however, released no funds and took no other action whatsoever. Instead, HUD assumed a litigation posture, responding through its attorneys that it was withholding payment under the contract and persisting in its claim of \$3.8 million against Hamilton. The contracting officer's inaction was a constructive denial of Hamilton's October 22nd claim for release of the withheld funds, which was appealable to this Court after December 22, 1997. The government's constructive denial of Hamilton's October 22, 1997 claim, by itself, is sufficient to vest jurisdiction in this Court.

Hamilton also submitted a deferment request by letter dated November 13, 1997. In addition to requesting "deferment of the alleged \$3,883.551 contract debt," Hamilton specifically requested that "HUD cease withholding all payments otherwise owed Hamilton under the Contract." (App., p. 70.) This letter, by itself or in combination with the October 22nd letter, also constituted a claim. Kalamazoo Contractors, Inc. v. United States, 37 Fed.Cl. 362, 368 (1997) (claim need not be in any particular format, and series of letters can be read together to constitute claim). The contracting officer constructively denied this claim because she took no action on it despite its pendency for over 60 days. Accordingly, the contracting officer's denial of the November 13th claim likewise provides a separate basis for establishing jurisdiction over the set off claim in this Court.

Hamilton's Claims Are Not Barred By The District Court Litigation

The government contends that jurisdiction is barred by the "in litigation" rule, either because the district court litigation precluded a decision on the December 10th claim or because the district court litigation was still pending when this suit was filed. Neither of these arguments has any merit.

The October 17th Government Claim Was Not Before The District Court

As shown above, the government asserted a final government claim against Hamilton for payment of \$3.8 million on October 17th. That claim was appealable to this Court, and it never was before the district court. The issue before the District Court – in Counts 1 and 2 of that action -- was whether HUD had taken the correct procedural steps to withhold payment of Hamilton's invoices totaling \$1.5 million.⁶ Here, the issue is whether HUD has any contractual basis to assert a claim for \$3.8 million. Thus, there was no identity of claims in litigation, and the filing of the district court action does not preclude jurisdiction in this Court. Case, Inc. v. United States, 88 F.3d 1004, 1010-1011 (Fed.Cir. 1996)

⁶ Counts 7 (constructive debarment) and 8 (due process violation) of Hamilton's district court action also alleged different claims than presented here. Accordingly, this action is not barred by those counts. Moreover, those counts referred to the withholding of funds only incidentally. Such incidental reference did not place the withholding issue in litigation under those counts. McDonnell Douglas, 37 Fed.Cl. 285, 289 n. 7 (1997); Cincinnati Electronics Corp. v. United States, 32 Fed.Cl. 496, 502 (1994). Finally, those counts were dismissed before this action was filed.

The District Court Action Was Dismissed Before This Action Was Filed

Moreover, the district court counts relating to withholding were voluntarily dismissed out on February 17, 1998 -- long before the instant action was filed on March 9, 1998. When Hamilton voluntarily dismissed Counts 1 and 2 pursuant to Fed.R.Civ.Pro. 41(a)(1) on February 17, 1998, those counts instantly were no longer "in litigation." Finley Lines Jt. Prot. Bd. Unit 200, Brotherhood of Railway Carmen, A Div. of Transport. Comm. Union v. Norfolk Southern Corp., 109 F.3d 993, 995 (4th Cir. 1997); Moore's Federal Practice § 41.33 (Matthew Bender 3d. ed.).⁷ Since the withholding claims were not in litigation, the Department of Justice did not have authority over them. Consequently, jurisdiction in this Court over the government's affirmative claim is not precluded by pre-existing litigation.

The December 10th Claim Was Constructively Denied Before the District Court Action Was Filed

By asserting a final claim for set off against Hamilton, the contracting officer also constructively denied Hamilton's affirmative claim for payment of outstanding invoices. Kit-San-Azusa, J.V. v. United States, 32 Fed.Cl. 647, 664 (1995) ("the CO's constructive denial of [the contractor's] claim for release of retainage was logically equivalent to granting the Government's claim to keep the

⁷ Although Rule 41(a) refers to dismissal of entire actions -- as opposed to individual counts -- the D.C. Circuit permits a plaintiff to "use Rule 41(a) to dismiss particular claims." Vail v. District of Columbia, 1988 WL 63069 n. 5 (D.D.C. 1988). In any event, Hamilton's Rule 41(a)(1) dismissal of Counts 1 and 2 constituted a constructive amendment of its Complaint, thereby removing those counts from litigation. Gronholz v. Sears, Roebuck and Co., 836 F.2d 515, 518 (Fed.Cir. 1987).

retainage"). Her constructive denial -- as of December 22nd -- of Hamilton's October 22nd claim for release of funds had the same effect. Consequently, Hamilton's December 10th claim was already constructively denied before the district court action was filed. Since the district court counts relating to withholding of funds also had been voluntarily dismissed (on February 17th) before this action was filed (on March 9th), the "in litigation" rule does not apply to preclude jurisdiction over Hamilton's claim for payment.

Different Claims Were Presented In The District Court Action

The result would be the same, even if it were assumed for sake of argument that Hamilton's December 10th claim was not constructively denied before January 8th. This is because the claims that were before the district court were not the same as the claim Hamilton submitted to the contracting officer on December 10, 1997. Since the claims were different, the contracting officer was never divested of jurisdiction over Hamilton's claim for payment of its invoices totaling \$1.5 million, and jurisdiction lies in this Court.

The situation here is akin to (and the reverse of) that in which a contractor appeals a default termination and then later sues for termination for convenience costs. The default termination appeal seeks declaratory relief (and sometimes remission of procurement costs), while the convenience termination suit seeks monetary damages. In such a situation, the Court is not divested of jurisdiction over the later-filed termination cost claim, even though there may be an overlap of factual and legal issues. See McDonnell Douglas Corp. v. United States, 37 Fed.Cl. 285,

290-291 (1997) (drawing a distinction between claims for declaratory relief and those for monetary damages in applying the "in litigation" rules).

Hamilton's December 10, 1997 claim was a demand for payment under the contract – a demand for monetary relief. It demanded payment of \$1.5 million based on HUD's improper withholding of payment and breach of contract. In contrast, Hamilton's district court action sought equitable declaratory and injunctive relief based on violations of the Administrative Procedure Act and the Due Process clause of the United States Constitution.

Although the two actions have some overlapping factual and legal issues, there is a fine distinction between them.⁸ The former focuses on contractual rights, while the latter concentrates on rights arising out of the Constitution and the APA. The contracting officer clearly had authority to decide the former, while she just as clearly had no authority to decide the latter. Conversely, the district court has authority to decide statutory and constitutional claims, but it had no authority to decide the contractual claims. 28 U.S.C. § 1346(a)(2). Thus, the district court's consideration of the statutory and constitutional claims before it did not impinge on the authority of the contracting officer to consider the contractual claims before her, and vice versa. The Department of Justice did not have the means to deprive the contracting officer of authority to render a final decision on Hamilton's CDA claim, and, thus, the CDA claim cannot be considered to have been in litigation before the district court. See Case, Inc., 88 F.3d at 1010-1011. Accordingly, Hamilton's December 10th claim was

⁸ The distinction is still important, since the "in litigation" rule must be narrowly construed. Hughes Aircraft Co. v. United States, 534 F.2d 889 (Ct.Cl. 1976).

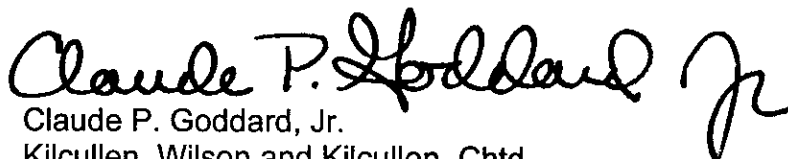
constructively denied by the contracting officer's failure to act on it within 60 days, and jurisdiction lies here on appeal from that constructive denial.

CONCLUSION

As shown above, jurisdiction exists over the government's set off claim against Hamilton pursuant to Placeway; jurisdiction lies over the contracting officer's constructive denial of Hamilton's October 22nd and November 13th claims, and Hamilton's December 10th claim was not in litigation so as to deprive the Court of jurisdiction. Accordingly, the government's motion to dismiss must be denied.

We respectfully request oral argument on the Motion.

Respectfully submitted,



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Kilcullen, Wilson and Kilcullen, Chtd.
1800 K Street, N.W.
Suite 300
Washington, DC 20006
Telephone: (202) 296-5700
Fax: (202) 296-5706

APPENDIX



U. S. Department of Housing and Urban Development
Washington, D.C. 20410-3000

OFFICE OF THE ASSISTANT SECRETARY
FOR ADMINISTRATION

OCT 17 1997

C. Austin Fitts
Hamilton Securities Advisory
Services, Inc.
7 Deepened Circle, NW
Washington, DC 20036-1108

Dear Ms. Fitts:

On Tuesday, October 14, 1997, I was apprised for the first time of two documents written by Hamilton Securities and/or Hamilton Securities Advisory Services, Inc. (hereinafter, "Hamilton") regarding Task Order 001 of Contract DU100C000018505. The first document is a DRAFT Memorandum dated December 4, 1996 and addressed to Kathy Rock, FHA Comptroller. The second document is a Report on Optimization dated December 20, 1996 and addressed to Nic Retsinas and Kathy Rock. These documents are unsigned, and were not provided by Hamilton to the Contracting Officer.

The documents detail erroneous instructions made by Hamilton with regard to the optimization requirements of the Task Order. Specifically, Hamilton states that it provided erroneous instructions to Lucent/Bell Labs, Hamilton's subcontractor, regarding optimization; that these instructions were not in accordance with the optimization model previously agreed to; and that Hamilton's erroneous use of the optimization model resulted in the selection of bidders that were not in accordance with the optimization model. Most importantly, Hamilton states in its December 20th Report on Optimization that it has determined, based upon detailed analysis of the errors, that HUD received \$3,883,551 less than it would have received had the awards been made in accordance with the optimization model approved by HUD.

I have thoroughly reviewed the contents of the referenced documents written by Hamilton. I find that they document Hamilton's failure to perform services required under the Task Order. Specifically, the Task Order Statement of Work at Sections 3.2, 6.1 and 6.2, requires the contractor to run the optimization model for the auctions and to deliver bids in accordance with the optimization model. By your own admission, Hamilton provided erroneous instructions that resulted in the Department suffering significant loss; a loss quantified by Hamilton at \$3,883,551. I find that this amount, at a minimum,

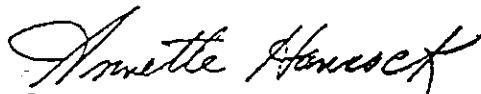
represents the monetary loss to HUD as a result of Hamilton's performance failure. However, the Government reserves the right to make future claims against Hamilton to recover any additional losses or damages the Department may suffer or has suffered as a result of Hamilton's failed performance.

In accordance with paragraph 32.610 of the Federal Acquisition Regulation, this letter is a demand for payment of the \$3,883,551 loss that the Department suffered as a result of Hamilton's performance failure. Your check, payable to the Department of Housing and Urban Development, should be forwarded to my attention in Room 5258, U.S. Department of Housing and Urban Development, 451 7th Street, SW, Washington, DC 20410-3000. If I do not hear from you within 10 work days, it is assumed you have determined not to make such voluntary repayment. The Department is currently withholding any further payments due and owing Hamilton under the terms and conditions of Contract DU100C000018505 and Task Order 001 until such time as the debt is satisfied.

Further, any amounts not paid within 30 days from the date of receipt of this letter will bear interest at the rate established by the Secretary of the Treasury, for the period affected, under Public Law 92-41. In addition, you may submit a proposal for deferment of collection if immediate payment is not practicable or if the amount is disputed.

Should you have any questions concerning the Department's demand for payment, please call me at (202) 708-1585, Ext. 133.

Sincerely,



Annette Hancock
Contracting Officer
Program Support Division
Office of Procurement and Contracts

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(847) 235-7810 FAX

202-639-6090

October 22, 1997

Ms. Annette Hancock
Contracting Officer
Program Support Division
Office of Procurement and Contracts
U.S. Department of Housing and Urban
Development
451 7th Street, S.W.
Room 5256
Washington, D.C. 20410

Dear Ms. Hancock:

We represent Hamilton Securities Advisory Services, Inc. (hereinafter "Hamilton") which until recently was the Department's chief outside financial advisor. By two letters dated October 17, 1997, your office terminated Hamilton's Contract No. -18505 for the Government's convenience and demanded payment of the sum of \$3.88 million. This letter addresses the second letter demanding a "voluntary repayment." Hamilton vigorously disputes the Government claim. It is apparent from the face of your letter that HUD did not discharge its duty to determine the contractual validity of the "debt" before asserting it. HUD's withholding contract payments otherwise due Hamilton, therefore, is improper.

At the outset several items merit mention.

First, your letter states that you personally were first apprised on October 14, 1997, of the Hamilton memorandum relating to the optimization discrepancy, thus implying that Hamilton previously hid the matter from HUD. Nothing could be further from the truth. When Hamilton became aware of the possibility of mis-communication concerning the bid "floors" employed with instructions relating to optimization models in certain HUD loan sales, Hamilton immediately brought the issue to the attention of senior HUD management. Hamilton's

disclosure was forthright and timely. The Hamilton documents of which you were "apprised" last week have been in HUD's hands for ten months. Moreover, the frank disclosure contained in these documents resulted not from any of the myriad investigations perpetually surrounding HUD, but rather was made voluntarily by Hamilton, compelled only by Hamilton's own integrity and honesty.

Second, the clear inference from your letter is that Hamilton's use of optimization somehow prejudiced the Department. That is not the case. Hamilton's pioneering use of optimization techniques in HUD loan sales have enhanced the value of the portfolio of mortgages sold, increased the likelihood of higher net value to the taxpayer and precluded large institutional firms from being solely eligible to win. The discrepancy disclosed by Hamilton does not impugn the use of computerized optimization in the least. The discrepancy affected only two of the nineteen sales in which Hamilton has been involved. Even as to the affected sales, the discrepancy did not somehow favor one class of bidders over another. And at worst, the discrepancy reduced revenues to HUD by less than 0.4% in the affected sales, and by 0.05% in all of the sales in which Hamilton was involved.

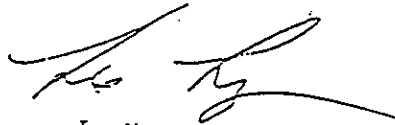
Third your letter demands, at a minimum, that Hamilton "voluntarily repay" the sum of \$3.88 million for Hamilton's alleged performance failure. This demand appears to be predicated on the notion that Hamilton acted as an underwriter and/or guarantor on mortgage sales. This is not the case. Hamilton acted as a financial advisor. Hamilton's performance under the Cross-Cutting Task Order met or exceeded the performance standards set forth in the task order, and did not violate the contractual provisions cited in the third paragraph of your letter. Moreover, the provisions you cite did not even apply to the West of Mississippi loan sale, which accounts for more than 60% of the worst-case impact of the optimization discrepancy. The demand also appears predicated on the notion that all winning bidders at mortgage sales/auctions close timely at the bid price submitted to the Department. That is not the case. The demand further appears predicated on the notion that Hamilton -- exclusively -- is contractually liable for the end results of the mis-communication. You make no mention of the role HUD or other financial advisors working on the affected sales might have had, nor do you even hint at any effort by HUD to consider such possibilities.

Fourth, your letter reserves "the right to make future claims against Hamilton." As we are sure you are aware, however, Hamilton has been the subject of a 15-month long IG investigation concerning allegations on topics ranging from bid-rigging to an alleged "relationship" between Ms. Fitts and a former HUD employee, Helen Dunlap. These allegations are unfounded. After a review of tens of thousands of documents, the investigation has turned up nothing. Yet the cost to Hamilton has been excessive. As a result of the convenience termination, Hamilton has laid off approximately half of its staff and lacks the money, personnel

and resources to embark on another 15-month investigative process related to voluntary repayments.

Lastly, the manner in which individuals at HUD and certain elements of the media have mounted a concerted assault on Hamilton is especially troubling. That your letter of Friday was leaked to the Washington Times around the time it was delivered to Hamilton amply confirms that politics remains the driving force behind HUD's actions and that fundamental fairness remains an anathema. Nevertheless, because Hamilton does not have the resources to deal with these continued assaults ad infinitum, we suggest the following. Legal representatives of your office and Hamilton should meet to discuss a method of settlement or alternative dispute resolution to resolve the demand and all other issues with the Department, once and for all. We do not believe that your demand is well-founded as a matter of contract law, but we are willing to attempt to resolve matters quickly and without litigation. In view of Hamilton's current financial condition and the magnitude of your demand, Hamilton will also submit a proposal for deferment of collection.

Sincerely,



Leslie H. Lepow
David A. Handzo

LHL/ksy

HAMILTON

November 13, 1997

Ms. Annette Hancock
Contracting Officer
Program Support Division
Office of Procurement and Contracting
U.S. Department of Housing and Urban Development
451 7th Street, SW
Washington, DC 20410

RE: Request for Deferment of Collection of Alleged Contract Debt Under:
Task Order 001, Contract No. DU100C000018505

Dear Ms. Hancock:

Pursuant to Federal Acquisition Regulation (FAR) 32.613, Hamilton Securities Advisory Services, Inc. and The Hamilton Securities Group, Inc. (collectively "Hamilton") hereby request deferment of collection of the alleged \$3,883,551 contract debt you have demanded and against which HUD is withholding contract payments otherwise owed Hamilton. As you know, Hamilton disputes the asserted debt. In light of Hamilton's present financial situation - a situation brought about by HUD's terminating Contract No. DU100000018505 (the "Contract") for the convenience of the government - deferment of collection is appropriate under the FAR. Further, as detailed below, deferment poses no risk to HUD's ability to collect in the event that a contract debt is determined to exist.

Pursuant to FAR 32.613(c), Hamilton submits the following information in support of this request:

(1) Financial condition.

As of October 31, 1997, Hamilton had cash balances and additional borrowing capacity under an existing bank line of credit of approximately \$500,000. Hamilton also had accounts receivable of approximately \$1.7 million. Receivables of approximately \$1.5 million for services rendered under the Contract are currently being withheld by HUD. Accounts payable and bank borrowings as of October 31, 1997 totaled approximately \$1.3 million. Hamilton currently has fewer than 20 employees.

(2) Contract backlog

Hamilton has no contract backlog

(3) Projected cash receipts and requirements

The termination of the Contract has had a significant impact on Hamilton's operations. Hamilton has restructured its operations and terminated approximately one-half of its workforce since the termination of the Contract. For the next several months, Hamilton projects that it will be operating at a monthly deficit of approximately \$400,000 per month. This monthly deficit will be funded through additional debt and/or high yield equity investments, and fees from asset management and broker dealer services.

(4) The feasibility of immediate payment of the debt

It is not feasible for Hamilton to pay immediately the alleged contract debt because of Hamilton's limited liquidity and current financial position. Should the contract debt be determined to exist, Hamilton holds an insurance policy which covers HUD's claim.

(5) The probable effect on operations of immediate payment in full.

As noted above, Hamilton currently has limited financial resources and liquidity. The immediate payment in full of this alleged contract debt would have a material adverse effect on Hamilton's ability to continue as a going concern and would render Hamilton insolvent and could result in involuntary bankruptcy.

As part of this deferment request, Hamilton requests that HUD cease withholding all payments otherwise owed Hamilton under the Contract. As you know, the Contract contains FAR Clause 52.246-25, Limitation of Liability - Services (April 1984). Under this clause, Hamilton is liable for the type of negligence and consequential damages alleged by HUD *only* to the extent of insurance coverage for such a claim. By the terms of the Contract, therefore, Hamilton otherwise cannot be held liable for the debt alleged. Hamilton holds an insurance policy potentially covering HUD's claim. Thus, HUD's deferring collection and ceasing withholding from Hamilton could not possibly impair HUD's ability to collect the alleged debt (if HUD's claim were determined to be valid), since the debt may be collected only to the extent it is covered by Hamilton's insurance policy. See FAR 52.246-25(c).

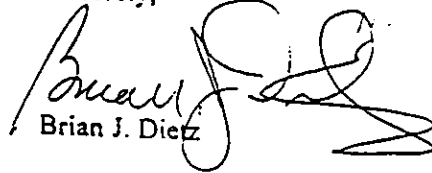
The FAR requires HUD, in considering this request for deferment of debt collection, to strike "a reasonable balance of the need for Government security against loss and undue hardship on the contractor." See FAR 32.613(e). In view of the Contract's Limitation of Liability clause (FAR 52.246-25), HUD's deferring collection and ceasing withholding will have absolutely no effect on the Government's security, since that security subsists solely (if properly at all) in Hamilton's insurance policy. On the other hand, the hardship imposed on Hamilton by immediate collection of the alleged debt would be dire. Under these circumstances, a "reasonable balance" of risks clearly indicates that the deferment request should be granted.

HAMILTON

Ms. Annette Hancock
November 13, 1997
Page 3

We are prepared to conclude a deferment agreement at your earliest convenience, and await your prompt response to this request.

Sincerely,



Brian J. Dietz

HAMILTON

December 10, 1997

Ms. Annette Hancock
Contracting Officer
Program Support Division
Office of Procurement and Contracts
U.S. Department of Housing and Urban Development
Washington, DC 20410-3000

RE: Contract Disputes Act Claim

Dear Ms. Hancock:

As you know, the U.S. Department of Housing and Urban Development ("HUD") currently is withholding all payments due and owed to Hamilton Securities Advisory Services, Inc. ("Hamilton") under Contract No. DU100C000018505 ("18505 Contract"). HUD is withholding payment on the following invoices submitted and currently payable under the 18505 Contract:

<u>Invoice Date</u>	<u>Invoice #</u>	<u>Amount Withheld</u>
9/26/97	17	\$868,417
10/23/97	18	\$636,839 ¹

This withhold, which relates to a claim by HUD for damages allegedly resulting from defective services provided by Hamilton under the 18505 Contract, is considered by Hamilton to be improper and is specifically in violation of the following: FAR 32.605(a)(2) and (b); 32.606(a), (b) and (c); 32.608(c); 32.610(b); and 32.613(b) and (d). Hamilton further believes that the withholding constitutes a breach of contract by the Government of the United States of America in that the Government has undertaken to collect certain monies from Hamilton with knowledge of the fact that the Government has no adequate basis for knowing the amount, if any, owed by Hamilton.

We also note that HUD has failed to respond to our November 13, 1997, Request for Deferment of Collection, which advised HUD that its withholding funds has caused and will continue to cause substantial and irreparable economic harm to Hamilton. The request pointed out that because, under the contract's Limitation of Liability - Services clause, HUD's alleged "claim" can exist only to the extent of Hamilton's insurance coverage and HUD's security

¹This amount is the pro rata portion of a regular monthly payment on the 18505 Contract (\$868,417) representing the period September 26 through October 17, 1997 (date of termination).

HAMILTON

Ms. Annette Hancock
December 10, 1997
Page 2

interests are protected entirely without withholding. HUD, therefore, can have no valid reason for continuing to withhold funds under the 18505 Contract.

Accordingly, claim is hereby made for the combined amount of \$1,505,256, plus interest from and after the date of this letter. Hamilton requests that a contracting officer final appealable decision be issued within the time provided by the Contract Disputes Act of 1978 and FAR Part 33, Subpart 2.

I certify that the claim is made in good faith; that the supporting data is accurate and complete to the best of my knowledge and belief; that the amount requested accurately reflects the contract adjustment for which the contractor believes the Government is liable; and that I am duly authorized to certify the claim on behalf of the contractor.

Sincerely yours,

Hamilton Securities Advisory Services, Inc.



By: C. Austin Fitts



HAMILTON

December 22, 1997

The Honorable Andrew M. Cuomo
U.S. Department of Housing and Urban Development
451 7th Street, SW
Washington, DC 20410-4500

Dear Secretary Cuomo:

I am writing this letter directly to you, at the same time that my company and its attorneys are talking to others at HUD, because I need you to take immediate action to prevent HUD's destruction of Hamilton.

Specifically, I am asking that you:

- authorize the release of checks to pay Hamilton on the two invoices that have been properly submitted for funds that are due and owing and which have been withheld for no reason authorized by law; and
- order the expeditious completion of audits that have been purposely delayed so that Hamilton can be paid remaining amounts legally due and to be paid subject to audit.

If you do not take this action, Hamilton will have to go out of business before HUD has instituted any legal action or given Hamilton its "day in court" over any pending dispute. While there may be those in your agency who desire this result, it violates law and subjects the agency to needless criticism and liability. HUD has ample procedures to review Hamilton's performance and actions lawfully, without it having to destroy it and without giving it a chance to defend itself.

If the amounts owed us are not released immediately, Hamilton will be unable to satisfy its obligations to its bank, its creditors and its employees. We have already laid off 28 employees since the cancellation of our contract with HUD, and we will have to lay off an additional 17 employees if the money you owe us is not forthcoming immediately. The impact on many people, whether employees, or our vendors and creditors, most of whom are consultants and small businesses, as well as Hamilton's bank and shareholders will constitute unnecessary and irreparable harm.

Hamilton has fulfilled all of its contractual obligations to HUD. We provided all services pursuant to a work plan subject to weekly reports and review. Our weekly reviews indicated that our performance was excellent. On October 17, 1997, following criticism of the Department's

HAMILTON

The Honorable Andrew M. Cuomo
December 22, 1997
Page 2

contracting process by the HUD Inspector General, and related coverage of such events by The Washington Times, you canceled Hamilton's contract for convenience with no notification and canceled procurements that were to replace our contract. This cancellation replaced a prior notification that the Department intended to cancel our contract for convenience when it had procured a replacement.

In each of these actions, HUD effectively short-circuited our plans and our ability to make alternative plans. We staffed our business to satisfy the work that your agency expected and we counted on the two years of payments under the contract to do so. When the contract was canceled, we then counted on an orderly process that was indicated for us to finish our work and make a transition to other projects. HUD's surprise announcements took from us our present funds and our ability to find new funds on a timely basis.

HUD's decision to withhold payment on the invoices that we have submitted seems to be based on its desire for a self-help set-off. Hamilton notified HUD last year of a mistake creating a discrepancy between the definition of floors in bidding packages and the bid modeling instructions. We were the ones to report the error and make an estimate of \$3.8 in net difference in proceeds. No claim was made by HUD at the time, and no action was required. Then months later, on the same day that the contract was canceled, HUD asked us for a "voluntary repayment" of \$3.8 million. Such a voluntary repayment is not provided for in the Act, your regulations, or in our contract.

HUD's action threatens our survival by taking from us funds that we need now, and it does so with no reason. We have repeated to your agency that we carry \$10 million of insurance should there be a claim that we committed an actionable error. Consequently, the self-help being taken now by your agency is without precedent or authority.

Here is why it is in your interest to pay us the \$1.5 million immediately and arrange for timely audit of our old outstanding invoices:

- HUD has no legal basis to withhold this money or to make a request for a voluntary repayment; HUD's insistence on this position sets a bad example for other contractors, makes the agency subject to litigation, and supports those who allege that HUD is retaliatory, punitive, and caters to political interference;
- HUD's release of funds and the expeditious audit will not impair the agency; HUD can be protected for any legitimate claim it has by the insurance policy in effect without putting Hamilton out of business; HUD's continued insistence on self-help actually will undermine its ability to collect on the merits if an actionable error actually occurred; and
- Hamilton's bankruptcy will not make it easier for HUD to press any legitimate claims it has, it will only make it more complicated.

HAMILTON

The Honorable Andrew M. Cuomo
December 22, 1997
Page 3

Your withholding of substantial revenues is the last of a long series of actions by HUD that seem to be intended to and will certainly have the effect of destroying Hamilton. For the last sixteen months, the public manner in which the HUD Inspector General has conducted her investigation of the loan sales program and Hamilton has systematically destroyed Hamilton's ability to do business with other federal agencies, recruit private clients, or conduct any trading business. In addition, the manner in which the HUD IG has conducted her investigation (e.g., service of overbroad and duplicative subpoenas) has substantially increased our cost of providing services under our contract to HUD, and added over \$1 million of legal and related investigation expenses to Hamilton. The impact on employee and subcontractor morale has been serious, causing physical, emotional and physical stress.

We had thought we would be free to rebuild our company after successfully completing our contractual obligations to HUD. We were wrong. Our contract termination included a request for several weeks more of effort to close out our work, delivering documents already in HUD's possession, many of which we have delivered to HUD on more than several occasions. We have been served with an additional overly broad subpoena and a follow-up request for yet more materials under earlier subpoenas. Also, my bank has been served with a subpoena for my personal financial records. Now it appears that the HUD IG's unethical suggestions of wrongdoing by Hamilton will prevent us from raising capital to proceed with our future businesses.

Last week our counsel, Jenner & Block, met with the Department of Justice to discuss our concerns regarding the manner in which the HUD IG is conducting its investigation of Hamilton. I have enclosed the letter that our attorneys sent to the Department that was the basis of the meeting. At that time, the Department of Justice attorney assigned to this matter agreed to call Howard Glaser, HUD's Deputy General Counsel, to recommend that moneys owed to Hamilton be "de-linked" from the HUD IG investigation.

Mr. Secretary, HUD has two choices. It can (with your involvement to make sure your agency follows the law) pay Hamilton what is legally owed to it on a timely basis. Or, the agency (if you should chose to ignore my plea) can cause Hamilton's bankruptcy, with the collective and personal responsibility for doing so (now that you too have been put on notice of the imminent problem we are facing). Having served at HUD myself and having this same choice to make from time-to-time, I am suggesting that your and the Department's short and long-term contract, policy, and legal interests are best served by meeting your contractual obligations.

HAMILTON

The Honorable Andrew M. Cuomo
December 22, 1997
Page 4

Please let me know immediately what your decision is. I and Hamilton's attorney's are available to meet at any time today.

Sincerely Yours,



~~C. Austin Fitts~~
Chairman

Enclosure

cc: Leslie H. Lepow, Esquire
David A. Handzo, Esquire
Abbe D. Lowell, Esquire
Howard Glaser, Esquire
Jon Cowan
Nicolas Retsinas
Willie Gilmore
John Opitz, Esquire
John Kennedy, Esquire
Annette Hancock
Susan Gaffney
Franklin Raines
G. Edward DeSeve
F. Stevens Redburn

LAW OFFICES

JENNER & BLOCK

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LESLIE H. LEPOW

December 22, 1997

Writer's Direct Dial: (202)639-6090
Writer's Internet Address: llepow@jenner.com

Howard Glaser, Esquire
Deputy General Counsel
Room 10214

BY HAND DELIVERY

John P. Kennedy, Esquire
Associate General Counsel for
Finance and Regulatory Enforcement
Room 9256

Office of General Counsel
U.S. Department of Housing and Urban Development
451 7th Street, S.W.
Washington, D.C. 20410

Re: Hamilton Securities Advisory Services, Inc. ("Hamilton"); HUD's
Withholding of Payments Due Under Contract No. DU100C000018505

Gentlemen:

On behalf of our client, Hamilton Securities Advisory Services, Inc. ("Hamilton"), we have over the past few weeks repeatedly contacted your respective offices to schedule a meeting to discuss our client's financial plight resulting from HUD's wrongful withholding of contract payments. The withholding of this money has pushed our client to the brink of extinction. It is imperative that we meet this week to discuss this matter.

Howard Glaser, Esquire
John P. Kennedy, Esquire
December 22, 1997
Page 2

As we have repeatedly stated in correspondence to your offices and others at HUD in the past,¹ HUD's demand for a "voluntary repayment" of \$3.88 million is not a valid basis for withholding \$1.5 million of funds due Hamilton for contract services already performed.

Several points merit mention:

- HUD's legal basis for "claiming" \$3.88 million has never been articulated or accompanied by a Contracting Officer's decision, as required by the FAR;
- The Contracting Officer's letter requesting "voluntary repayment" cites as authority for the repayment demand a contract provision in a contract that was not in effect for one of the sales in which Hamilton's performance allegedly prejudiced HUD;
- The Department's claim appears predicated upon the notion that Hamilton functioned as a guarantor or indemnitor of the proceeds of loan sales. This is not the case, and to seek a liability based on such a theory is specious;
- The invocation by HUD sources of a Justice Department inquiry as a basis for the withholding is not justified, as was confirmed to us in a meeting with AUSAs Van Gelder, Alexis and Chapman on December 18, 1997, who stated that the two actions are not "linked";
- Lastly, literally two days before HUD terminated Hamilton's contract, HUD contracting officials informed Hamilton that it's most recent invoice of \$868,000 would be approved for payment

Significantly, as we have repeatedly pointed out to the Department, without conceding any basis for liability, the alleged performance errors by Hamilton are covered by insurance in the event of an ultimate determination of liability. In other words, HUD has already been rendered secure.

¹ See Letter of October 22 from the undersigned to HUD's Contracting Office (Annette Hancock), November 13 from Hamilton (CFO - Brian Dietz) to HUD's Contracting Office, December 12 from the undersigned to John Kennedy, HUD's Associate General Counsel.

Howard Glaser, Esquire
John P. Kennedy, Esquire
December 22, 1997
Page 3

HUD's steadfast refusal to meet with us and the simultaneous withholding of funds due under a fixed price contract can only be, therefore, for the purpose of punishing Hamilton, clearly not for any contractual purpose. Such action is fundamentally unfair and will cause irreparable injury.

We reiterate our desire to meet with you as soon as possible to discuss the release of funds to Hamilton.

Sincerely,



Leslie H. Lepow

LHL/ef

cc: Ms. C. Austin Fitts
David A. Handzo, Esquire
Ms. Annette Hancock
Barbara Van Gelder, Esquire
Anthony Alexis, Esquire
Richard Chapman, Esquire
John Opitz, Esquire



HAMILTON

December 29, 1997

Howard Glaser, Esq.
Deputy General Counsel
U.S. Department of Housing and Urban Development
Office of General Counsel
451 7th Street, SW
Room 10214
Washington, DC 20410-4500

RE: Hamilton Securities Advisory Services, Inc.; HUD's
Withholding of Payments Due Under Contract No. DU100C000018505

Dear Mr. Glaser:

The U.S. Department of Housing and Urban Development ("HUD") is wrongfully withholding contract payments due to Hamilton Securities Advisory Services, Inc. ("Hamilton") totaling \$1,505,256. Members of the Office of General Counsel have communicated that are two reasons why HUD has taken this action:

- there is an ongoing investigation and HUD has been requested to withhold Hamilton's contract payments until the investigation is completed; and/or
- HUD is withholding the contract payments as security for HUD's \$3.88 million claim for a "voluntary repayment" by Hamilton because Hamilton has not provided sufficient evidence that it carries insurance that could cover this claim.

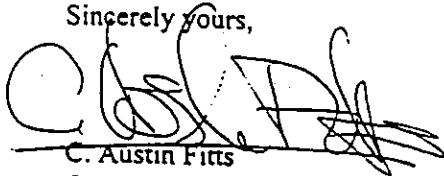
Over the past few weeks our attorneys at Jenner & Block have addressed your concerns as follows:

- On December 18, 1997, Jenner & Block met with Assistant US Attorneys Van Gelder, Alexis and Chapman. At that meeting, the Department of Justice indicated that any investigation and the withholding by HUD of contract payments to Hamilton are not "linked," so that the existence of an investigation is not a basis for withholding the contract payments, and agreed to call you to confirm that these payments should be delinked; and
- A copy of Hamilton's professional liability insurance policy was provided to Mr. John Kennedy of the HUD Office of General Counsel on December 12, 1997. In addition, on December 23, 1997, Mr. Kennedy was provided with a letter from Jenner & Block which confirmed with our professional liability insurance carrier that HUD's claim, in the event of an ultimate determination of liability against Hamilton, is covered by a \$10 million per claim

professional liability policy. Please see enclosures. The insurance company is available to confirm this verbally with Mr. Kennedy at his convenience.

We presume that the above successfully addresses the causes that led you to withhold our contract payments. Accordingly, we request that you authorize immediate payment to Hamilton of the \$1,505,256 being withheld by HUD. In addition, we request that a check be processed immediately so that we may pick it up today. Failure to do so before the end of the year will cause irrevocable harm to Hamilton, its employees and its creditors.

Sincerely yours,



C. Austin Fitts
Chairman

cc: The Honorable Andrew Cuomo
Mr. Jon Cowan
John Opitz, Esquire
John Kennedy, Esquire
Mr. Willie Gilmore
Mr. Nicolas Retsinas
Mr. Dwight Robinson
Ms. Annette Hancock
Mr. Craig Durkin

Enclosures



OFFICE OF GENERAL COUNSEL

December 30, 1997

C. Austin Fitts, Chairman
Hamilton Securities Group, Inc
7 Dupont Circle, NW
Washington, Dc 20036

Dear Ms. Fitts:

I am in receipt of your letter of December 29, 1997. Because I believe there are misperceptions in the letter, I am responding immediately. However, due to the complexity of the issues involved, I will also supplement this response should it be deemed necessary.

As you are aware pursuant to Contracting Officer Annette Hancock's letter of October 17, 1997, the Contracting Officer recently discovered that Hamilton breached its contractual obligations owed to HUD and, as a result of those breaches, HUD suffered damages at least in the amount of \$3,883,551.

As you know, Hamilton has provided similar services to HUD under several different contracts. In Contracting Officer Hancock's letter of the October 17, 1997, she referred to Contract No. DU100C000018505. However, by letter dated October 22, 1997, your attorney, Les Lepow, provided clarification to Ms. Hancock that the alleged breaches occurred under two separate contracts, both Contract No. DU100C000018505 and Contract No. DU100C000018161. Thus, there are at least two contracts at issue in this matter.

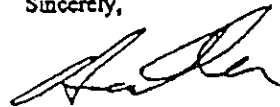
In November, Ms. Austin Fitts sent a letter to the Contracting Officer requesting deferment of the debt. It is my understanding that the Contracting Officer will be responding to that request shortly. Although Hamilton at least in part based its request on the existence of insurance, Hamilton had not as of that time provided the insurance policies to the Contracting Officer. Subsequently, Mr. Lepow sent to Associate General Counsel John Kennedy an insurance policy pertaining to Contract No. DU100C000018505. This should assist the Contracting Officer in having some of the information she needs to make her decision regarding deferment. (Yet, as noted above, the alleged contract breaches also pertained to Contract No. DU100C000018161, and I do not believe that any insurance policy pertaining to that contract has been forwarded to the Contracting Officer or HUD.)

In response to concerns expressed in your December 29, 1997 letter, I note that HUD has engaged in withholding and/or set-off, in accordance with law, based upon the fact that Hamilton is indebted to HUD due to breach of contract. HUD is exercising its common law right, and right in accordance with the Federal Acquisition Regulations, to withhold and/or set-off the debt. We have uncovered nothing in either Contract No. DU100C000018161 or DU100C000018505 which would preclude HUD from exercising these rights to satisfy the debt. Furthermore, Hamilton has not articulated legal or factual bases as to why HUD may not exercise these rights. If Hamilton wishes to submit legal and/or factual proof supportive of the following (or otherwise supportive of its position), then HUD will take them into consideration, as appropriate: (1) The existence of insurance policies which may be used to fully satisfy the debt; and (2) the basis for Hamilton's allegation that the existence of one or more insurance policies preclude HUD from exercising its right to set-off and/or withholding.

In working towards resolution of pending matters between HUD and Hamilton, I believe it would prove helpful if the different individuals representing or acting on behalf of Hamilton were to coordinate their responses to HUD. I note that, since the October 17, 1997 letter from Ms. Hancock, there have been different, somewhat conflicting responses from Hamilton. For example, Mr. Les Lepow telephoned Assistant General Counsel Opitz indicating his desire to engage in settlement negotiations with HUD on behalf of Hamilton with regard to the alleged debt. By letter dated October 22, 1997 to Ms. Hancock, Mr. Lepow also stated that he represented Hamilton in this matter. Yet, independently, HUD has received correspondence from both Mr. Brian Dietz and Ms. Austin Fitts which each appear to take different stances on behalf of Hamilton with regard to the various issues. It is unclear if Mr. Dietz and Ms. Fitts are acting in coordination with Mr. Lepow, and who is the representative for Hamilton.

Thank you for your consideration in this matter. I look forward to meeting with representatives of Hamilton on Friday, and receiving any additional information which you may have supportive of your position.

Sincerely,



Howard Glaser
Deputy General Counsel



U.S. Department of Justice
Civil Division
Commercial Litigation Branch

David J. Gonsky

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March 6, 1998

BY FAX (202/737-7565)

Mr. David E. Frulla
Brand, Lowell & Ryan
923 15th Street NW
Washington, DC 20005

Re: Hamilton Securities v. HUD

Dear David:

This is to remind your clients, Hamilton Securities Group, Inc. and Hamilton Securities Advisory Services, Inc. (collectively, "Hamilton"), their officers and other representatives of the effect of the Federal Priority Statute, 31 U.S.C. § 3713, and other applicable laws with regard to the disposition of Hamilton's assets and funds. We have learned that Hamilton plans to sell various of its assets at an auction on March 10, 1998. The laws to which we refer in this letter might have particular impact on the disposition of proceeds from the sale of such property.

We have directed this letter to you on the assumption that you represent Hamilton with regard to the subject matter discussed herein. If that is not so, please inform us and pass this letter along to Hamilton and any counsel who represents it with regard to this matter.

1. The Government's Claim

By prior correspondence, the United States Department of Housing and Urban Development ("HUD") demanded that Hamilton pay HUD \$3,883,551.00, based upon certain failures by Hamilton to perform properly under contracts involving the sale of HUD-held mortgages. While this figure was based upon admissions and information supplied by Hamilton, independent analysis by HUD might result in demands for additional amounts. HUD has withheld payment of \$1,505,256 claimed by Hamilton as contract payments, pending possible recoupment or setoff by HUD.

After netting the above figures, Hamilton still owes HUD at least \$2,378,295.

2. The Federal Priority Statute

The Federal Priority Statute, 31 U.S.C. § 3713, provides in pertinent part:

"Priority of Government claims

(a) (1) A claim of the United States Government shall be paid first when—

(A) a person indebted to the Government is insolvent and—

(i) the debtor without enough property to pay all debts makes a voluntary assignment of property;

(ii) property of the debtor, if absent, is attached; or

(iii) an act of bankruptcy is committed;

* * *

(b) A representative of a person or an estate (except a trustee acting under title 11) paying any part of a debt of the person or estate before paying a claim of the Government is liable to the extent of the payment for unpaid claims of the Government."

Thus, for example, if any representative of Hamilton uses proceeds from the upcoming auction to pay debts other than those permitted to be paid under this statute before satisfying the Government's claim, such representative might be personally liable to the Government for the amount of the payment.

3. Other Laws

Other laws also might restrict Hamilton's ability to dispose of assets or monies prior to complete satisfaction of the debt to the Government. We do not undertake to list all possible laws that might apply, but please pay particular attention to laws concerning fraudulent conveyances, such as those found in the Federal Debt Collection Procedures Act, 28 U.S.C. § 3301 *et seq.*

If you have any questions, please do not hesitate to call us.

Very truly yours,



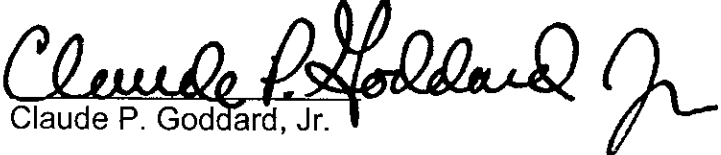
DAVID J. GOTTESMAN
Trial Attorney
Commercial Litigation Branch
Civil Division

Certificate of Service

The undersigned certifies under penalty of perjury that he caused a copy of the foregoing Motion to be served on the following government counsel by hand on June 25, 1998:

David J. Gottesman
Attorney
Commercial Litigation Branch
Civil Division
United States Department of Justice
Washington, D.C. 20005

Attn: Classification Unit
8th Floor, L Street Building


Claude P. Goddard, Jr.